

Proposed Hawaii Administrative Rules
Hearing Date: January 6, 2016

DEPARTMENT OF TAXATION

Amendments to Chapter 18-235,
Hawaii Administrative Rules

_____, 2015

SUMMARY

1. Section 18-235-5-02 is amended.
2. Section 18-235-5-05 is added.
3. Section 18-235-38-01 is amended.

§18-235-5-02 Allocation and separate accounting.

(a) Taxpayers described in section 18-235-5-01(b) who are required to determine Hawaii source income shall determine Hawaii source income by allocation and separate accounting so far as practicable as required by section 235-5(b), HRS.

(1) If the nature of the taxpayer's activity renders direct allocation impracticable, or the taxpayer's books of account and records do not clearly reflect income properly taxable by Hawaii, income shall be allocated or apportioned under sections 235-21 to 235-39, HRS.

(2) If the taxpayer's activity within the State is an integral part of a unitary business carried on within and without the State, income shall be allocated or apportioned under sections 235-21 to 235-39, HRS. For purposes of this paragraph, "integral part of a unitary business" means the activity is central to the activity of the taxpayer such that allocation and separate accounting is not practicable.

(b) When the separate accounting method is used, separate records shall be maintained for sales, cost of sales, and expenses which are attributable to activity within Hawaii. Overhead expenses not directly allocable to activity within or without Hawaii shall be allocated according to the facts and circumstances, and in conformity with generally accepted accounting principles.

(c) A change in the taxpayer's allocation method or apportionment formula is a change in the taxpayer's method of accounting within the meaning of sections 446 (with respect to methods of accounting) and 481 (with respect to adjustments required by changes in method of accounting) of the Internal Revenue Code of 1986, as amended. [Eff 2/16/82; am and renum §18-235-5-02 9/3/94; am] (Auth: HRS §§231-3(9), 235-118) (Imp: HRS §235-5)

§18-235-5-05 Alternative apportionment. (a) As authorized by section 235-5(e), HRS, if the director of taxation determines that the method set forth in section 235-5, HRS, and administrative rules thereunder does not fairly determine income derived from or attributable to Hawaii, or does not clearly and accurately reflect the actual amount of income received from all property and sources within the State, the director may permit or require:

- (1) Separate accounting;
- (2) The exclusion of any one or more of the factors;
- (3) The inclusion of one or more additional factors which will fairly represent the taxpayer's business activity in this State; or
- (4) The employment of any other method to effectuate an equitable allocation and apportionment of the taxpayer's income.

(b) A taxpayer may petition the director to use an alternative apportionment method pursuant to section 235-5(e), HRS, by written request.

- (1) The petition shall include data clearly showing that the application of factors provided in the law, including these rules, does not result in a reasonable attribution of net income to Hawaii due to the peculiar nature of the taxpayer's business and that the taxpayer's proposed method more clearly reflects income attributable to Hawaii.
- (2) The petition shall disclose the extent to which the proposed method is being used in other states to which the taxpayer reports.

(c) The following shall be sufficient to constitute the director's imposition of alternative apportionment under this section:

- (1) Issuance of an assessment based on an alternative method accompanied by notification that an alternative method was used;
- (2) For a claim for refund on an original return, denial of a taxpayer's claim for

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- refund accompanied by notification that an alternative method was used;
- (3) For a claim for refund made via an amended original return, denial of a taxpayer's claim for refund without more, provided that the alternative used by the director consists wholly of the method used by the taxpayer in filing its original return.
 - (4) In all other cases, any notification that an alternative method was used. [Eff
] (Auth: HRS §§231-3(9), 235-118) (Imp: HRS §235-5)

§18-235-38-01 Equitable adjustment of apportionment formula.

(a) If the director of taxation determines that the apportionment formula prescribed by section 235-29, HRS, does not fairly determine net income derived from or attributable to Hawaii, the director may direct or permit the use of an apportionment formula based on other factors that would more clearly reflect income attributable to Hawaii.

(b) A taxpayer may petition the director to use an allocation or apportionment method other than that prescribed in part II of chapter 235, HRS, by written request.

(1) The petition shall include data clearly showing that the application of factors provided in the law, including these rules, do not result in a reasonable attribution of net income to Hawaii due to the peculiar nature of the taxpayer's business and that the taxpayer's proposed method more clearly reflects income attributable to Hawaii.

(2) The petition shall disclose whether the method that is being used or requested is being employed in all other states to which the taxpayer reports under Article IV of the Multistate Tax Compact or the Uniform Division of Income for Tax Purposes Act.

(c) The following shall be sufficient to constitute the director's imposition of alternative apportionment under this section:

(1) Issuance of an assessment based on an alternative method accompanied by notification that an alternative method was used;

(2) For a claim for refund on an original return, denial of a taxpayer's claim for refund accompanied by notification that an alternative method was used;

(3) For a claim for refund made via an amended original return, denial of a taxpayer's claim for refund without more, provided that the alternative used by the director

- consists wholly of the method used by the taxpayer in filing its original return.
- (4) In all other cases, any notification that an alternative method was used." [Eff 11/25/94; am] (Auth: HRS §§231-3(9), 235-118) (Imp: HRS §§235-38, 235-117)